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**IMPACT OF MONETARY POLICY RATE CHANGES ON COMMERCIAL BANK LENDING
IN NIGERIA**

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Abstract

This study looks at how changes in monetary policy affected commercial bank lending in Nigeria from 1992 to 2024. The monetary policy rate, inflation rate, cash reserve ratio, and liquidity ratio were used as proxies for monetary policy attitude, while commercial bank lending was represented by total credit to the private sector. The Central Bank of Nigeria (CBN) Statistical Bulletin was the main source of secondary data. In terms of methodology, the study used the Auto-Regressive Distributed Lag (ARDL) framework to determine both short- and long-term correlations among the variables and the Augmented Dickey-Fuller (ADF) test to determine stationarity. Both the loanable funds theory and the monetary transmission mechanism theory served as the foundation for the investigation, with the former serving as the primary framework. Monetary policy has a major long-term impact on bank loans, according to empirical data. In particular, the contractionary impact of price instability and prudential constraints was reflected in the negative but statistically significant effects that inflation and the liquidity ratio had on loans to the private sector. On the other hand, bank lending and the monetary policy rate showed a strong and positive correlation, indicating the monetary policy rate's efficacy as a policy lever in credit distribution. Despite being positively signed, the cash reserve ratio was statistically insignificant, suggesting a modest channel of effect. The study comes to the conclusion that changes in monetary policy have a significant impact on the flow of credit to the private sector, with possible trade-offs between credit expansion and financial stability. It suggests that the CBN maintain a balanced policy mix that protects price stability and macroeconomic sustainability while encouraging credit expansion.

Keywords Monetary Policy Rate, Inflation, Cash Reserve Ratio, Liquidity Ratio, Credit to Private Sectors.

Introduction

In Nigeria's financial landscape, the cost of borrowing from commercial banks has become a mirror of broader macroeconomic tensions. The lending rate—long a barometer of credit conditions—has in recent months reflected a tightening grip by monetary authorities. By March 2025, the average lending rate stood at 17.96 percent, slightly easing from 18.35 percent in February, yet masking a more severe reality where maximum lending rates across banks reached as high as 30.28 percent in late 2024, the highest in nearly two years. These figures reveal the complex interplay between monetary policy stance and the willingness and capacity of banks to extend credit. In Nigeria, commercial bank lending is not merely a mechanical process of disbursing loans but a delicate balance between liquidity management, risk assessment, and policy constraints. As conceived by this study, commercial bank lending refers to the process by which deposit money banks provide credit facilities—such as loans, advances, overdrafts, and other forms of financing—to individuals, businesses, and government entities, with the intent to stimulate economic activities while ensuring repayment through collateral, interest charges, and contractual agreements.

Ofoegbu (2024) highlights that bank lending continues to be the main source of external financing for businesses in emerging economies like Nigeria, making it a crucial driver of growth. Ejem and Nwosu (2023) highlight its role as the primary channel for mobilising savings into productive investment. The monetary policy rate, which acts as the anchor for all other interest rates in the economy, is a crucial factor in determining lending conditions. This research defines monetary policy rate changes as the Central Bank of Nigeria's (CBN) intentional modifications to its benchmark interest rate with the goals of affecting credit availability and cost, managing inflation, and preserving currency stability. Ibe and Osuji (2024) assert that the monetary policy rate serves as a signal to the financial system, influencing credit demand and banks' lending rates. The CBN has been on an aggressive tightening cycle over the previous year, raising the monetary policy rate by 875 basis points between 2023 and early 2025 before keeping it at 27.5 percent in February 2025. A high cash reserve ratio of 50% and a liquidity ratio of 30% have been implemented in tandem with these policy changes, which directly restrict banks' ability to lend.

There are several mechanisms that mediate the link between changes in monetary policy rates and commercial bank lending. The cost of funding for banks increases as the monetary policy rate rises, and this is transferred to borrowers through higher lending rates, which reduces the demand for credit. Such tightening is frequently necessary to reduce buying power and stabilise the naira due to inflation, which averaged over 33 percent in late 2024. However, this has the unintended consequence of limiting credit expansion to the private sector. Similar to how a strict liquidity ratio forces banks to keep a large percentage of liquid assets, further limiting credit creation, an increased cash reserve ratio locks up a significant amount of bank deposits with the CBN, restricting liquidity available for lending. Adeleke and Yusuf (2023) contend that these processes are a component of the interest rate transmission channel of monetary policy, which allows policy choices to affect borrowing costs and investment choices, which in turn affect the real economy.

The sensitivity of Nigerian bank lending to shifts in monetary policy is supported by empirical data. While Chukwu and Eze (2023) found that extended periods of high interest rates correlate with decreased loan accessibility for small and medium-sized businesses, Okafor and

Agu (2024) found that a one percentage point increase in the monetary policy rate significantly reduces private sector credit growth in the following quarter. There are still gaps in the literature, nevertheless. The long-term dynamics between monetary policy components—such as the policy rate, cash reserve ratio, liquidity ratio, and inflation—and commercial bank lending are understudied since many current research concentrate on short-term impacts. Furthermore, the amount of knowledge required for targeted monetary and credit strategies is limited since sectoral differences in credit reaction to policy changes are rarely addressed. Therefore, by empirically evaluating the effects of monetary policy rate changes on commercial bank lending in Nigeria, this study aims to close this gap and provide new insights based on current trends and macroeconomic reality.

Literature Review

Conceptual Literature

Monetary Policy Rate

A country's macroeconomic framework depends heavily on the monetary policy rate, which directs changes in interest rates and affects lending, borrowing, and investment choices. It is commonly acknowledged as the benchmark interest rate that informs financial markets and the general economy of the central bank's monetary position. The rate at which the central bank loans to deposit money banks serves as the anchor for other interest rates in the economy, according to Adebayo and Olayemi (2021). According to Eze and Okonkwo (2022), it is the main weapon that the monetary authority uses to control inflation, manage the money supply, and stabilise the currency, all of which have an impact on overall economic growth. In a similar vein, Nwachukwu (2023) describes the monetary policy rate as a signalling tool that conveys monetary policy objectives to the banking industry, influencing aggregate demand and credit conditions. According to the Central Bank of Nigeria (CBN, 2024), it is the benchmark interest rate that serves as a reference for other economic rates, influencing liquidity circumstances and preserving macroeconomic stability. According to this study, the Central Bank of Nigeria sets the monetary policy rate, which is the strategic interest rate that serves as a direct lever and a signalling mechanism to affect commercial bank lending rates, credit creation, and liquidity levels in the economy. In the context of this study, it is viewed as a crucial factor influencing credit availability, investment flow, and Nigeria's overall economic performance in addition to being a macroeconomic management tool.

Monetary Policy Rate Changes

Changes in the benchmark interest rate that a nation's central bank sets to affect financial market conditions, economic activity, and macroeconomic stability are referred to as monetary policy rate changes. Usually, these adjustments are used to control inflation, promote economic expansion, or reduce excessive liquidity. Ezeaku (2021) asserts that changes in the monetary policy rate have a direct impact on the lending practices of commercial banks since lower rates promote credit growth while higher rates often restrict borrowing. In a similar vein, Nwokoye and Agu (2022) observe that changes in monetary policy rates act as a signalling mechanism, directing market expectations and impacting inflationary trends, asset prices, and currency rates. Similarly, Okonkwo et al. (2023) claim that the speed and scope of monetary transmission are determined by the size and frequency of MPR shifts, which in turn influences investment choices and consumption trends in the economy. For the purposes of this study,

monetary policy rate changes are defined as regular upward or downward adjustments in the Central Bank of Nigeria's policy rate with the goal of controlling inflation, regulating the cost of credit, and maintaining macroeconomic balance. These changes have a direct impact on the lending practices of commercial banks and overall economic activity.

Lending from Commercial Banks

The process by which deposit money banks provide credit facilities to people, companies, and governmental organisations, mostly for working capital, investment, and consumption, is known as commercial bank lending. By directing financial resources to profitable industries, banks play a crucial role in promoting economic progress. Adebayo and Olayemi (2021) define commercial bank lending as the distribution of cash by banks to eligible borrowers under predetermined conditions, with interest charges and repayment responsibilities serving as the transaction's foundation. In a similar vein, Ume and Eze (2022) characterise it as an essential intermediation activity in which banks transfer deposits from surplus units to deficit units in order to boost economic activity. Similarly, Okoro and Ibrahim (2023) claim that commercial bank lending is essential to financial deepening, impacting investment trends, employment growth, and general economic stability. For the purposes of this study, commercial bank lending is defined as the act of deposit money banks extending credit to people, businesses, and governmental organisations with the main goals of promoting macroeconomic stability, encouraging economic growth, and enabling profitable investments.

Changes in Monetary Policy Rates and Commercial Bank Lending

One important way that monetary authorities affect credit availability and economic activity is through the link between changes in monetary policy rates and commercial bank lending. Commercial banks' cost of funds is strongly impacted by changes in the monetary policy rate, which in turn influences their lending rates, loan volumes, and risk tolerance. Eze and Okafor (2021) state that while a fall in the monetary policy rate tends to encourage lending by making credit more accessible, a rise in the rate usually boosts commercial banks' lending rates, discouraging borrowing and limiting credit development. Similarly, Olayemi and Adegbite (2022) point out that variables including liquidity circumstances, inflation expectations, and banks' capital adequacy operate as mediators in the transmission of monetary policy rate changes to commercial bank lending. Accordingly, Ibrahim and Musa (2023) contend that changes in monetary policy rates have a major impact on the amount and sectoral distribution of bank lending and are the main monetary policy instrument for managing inflation and stabilising the economy. The dynamic interaction in which changes in the monetary policy rate impact commercial banks' lending practices, interest rate structures, and credit allocation patterns—thereby influencing investment, consumption, and overall economic performance—is how the relationship between monetary policy rate changes and commercial bank lending is conceptualised for the purposes of this study.

Theoretical Literature

Monetary Transmission Mechanism Theory

Changes in the benchmark interest rate that a nation's central bank sets to affect financial market conditions, economic activity, and macroeconomic stability are referred to as monetary policy rate changes. Usually, these adjustments are used to control inflation, promote economic expansion, or reduce excessive liquidity. Ezeaku (2021) asserts that changes in the

monetary policy rate have a direct impact on the lending practices of commercial banks since lower rates promote credit growth while higher rates often restrict borrowing. In a similar vein, Nwokoye and Agu (2022) observe that changes in monetary policy rates act as a signalling mechanism, directing market expectations and impacting inflationary trends, asset prices, and currency rates. Similarly, Okonkwo et al. (2023) claim that the speed and scope of monetary transmission are determined by the size and frequency of MPR shifts, which in turn influences investment choices and consumption trends in the economy. For the purposes of this study, monetary policy rate changes are defined as regular upward or downward adjustments in the Central Bank of Nigeria's policy rate with the goal of controlling inflation, regulating the cost of credit, and maintaining macroeconomic balance. These changes have a direct impact on the lending practices of commercial banks and overall economic activity.

Theory of Loanable Funds

According to the Loanable Funds Theory, which was created by Wicksell in 1898 and further improved by Robertson in 1934 and Ohlin in 1937, the economy's supply and demand for loanable funds interact to determine interest rates. Savings, dishoarding, bank credit creation, and capital inflows are the sources of loanable funds, while government borrowing, investment, and credit-financed consumption are the sources of demand. The theory makes the following assumptions: that the interest rate flexibly adjusts to equilibrate the market for loanable funds; that savings rise with higher interest rates while investment falls; and that there is a free and open exchange between lenders and borrowers in a competitive capital market. Additionally, it makes the assumption that the availability of these funds may be influenced by monetary circumstances, indicating that money is not neutral in the short term. By taking into consideration the function of bank credit creation and monetary impacts in addition to savings and investment flows, proponents like Robertson (1934) and Ohlin (1937) contend that the theory provides a more thorough framework than the classical theory.

According to contemporary academics like Mishkin (2019), the theory is still applicable in describing how central banks affect the market for loanable funds and, consequently, the behavior of commercial lenders through tools like the cash reserve ratio, monetary policy rate, and open market operations. However, others have questioned the assumptions of the hypothesis. Through his Liquidity Preference Theory, Keynes (1936) contended that business expectations and liquidity preferences had a greater influence on investment choices than interest rates alone. Robinson (1956) and other Post-Keynesians argued that the idea that savings must come before lending is undermined by the theory's failure to account for the reality of endogenous money creation in contemporary banking, where loans themselves generate deposits. The Loanable Funds Theory offers a helpful perspective for analyzing how changes in monetary policy affect commercial bank lending in Nigeria. The cost of borrowing is impacted by changes in the monetary policy rate, which in turn affects the demand for loanable money from consumers and enterprises. Concurrently, the amount of money available for banks to lend is directly impacted by policy instruments like the liquidity ratio and cash reserve ratio. Recent events in Nigeria have shown that persistently high monetary policy rates combined with high cash reserve requirements have reduced liquidity, increased lending rates, and limited credit availability. Therefore, this theoretical approach provides important insight into the link between policy changes and credit supply in an economy that significantly depends on bank intermediation by capturing the process via which monetary policy choices impact lending outcomes in the banking sector.

Empirical Review

Akinlo and Apanisile's (2023) study looked at the Monetary Policy Rate and Commercial Bank Lending in Nigeria. The money supply, exchange rate, inflation rate, and monetary policy rate were all included as independent variables in the study. The amount of loans that commercial banks made to the private sector served as the dependent variable. Every three months, the Autoregressive Distributed Lag (ARDL) bounds testing method was used to data from 2000 to 2022. This study found that changes in monetary policy rates eventually make bank lending more challenging. A statistically significant adverse effect is present. Nonetheless, the short-term consequences of inflation and the currency rate were both favourable and unfavourable. According to the study, banks have a harder time extending loans when the MPR keeps rising. Furthermore, Okonkwo and Uche (2023) looked into how shifts in Nigeria's monetary policy rates affect how private banks distribute money. The GDP, money supply, inflation rate, and monetary policy rate (MPR) were used as independent variables. Commercial bank loans and advances were the dependent variable. Using quarterly data from 2000 to 2022 using the Autoregressive Distributed Lag (ARDL) bounds testing technique, the study found that while GDP growth had a favourable effect on the credit supply, MPR had a substantial long-term negative impact on bank loans. The amount of money in the economy was positively and significantly correlated with inflation, notwithstanding the short-term negative impacts of inflation. Nigeria needs stable and reliable MPR laws to sustain credit development, according to the study's conclusions.

Okoye and Eze (2022) looked into how Nigeria's monetary policy affects banks' lending practices. In this study, the government bill rate, cash reserve ratio, liquidity ratio, and monetary policy rate were all regarded as independent variables. On the other hand, loans and advances from commercial banks were regarded as the dependent variable. Using annual data from 1990 to 2020 and the Vector Error Correction Model (VECM), the results showed that banks loaned much less when the MPR and CRR grew but considerably more when the liquidity ratio increased. The authors contend that when monetary policy is more strict, banks are unable to extend as much credit. In a similar vein, Afolabi and Ogunleye (2022) looked at how changes in monetary policy affected bank loans to Nigeria's private sector. Private sector credit was the dependent variable in their research, whereas the MPR, exchange rate, inflation, and cash reserve ratio were the independent factors. They found that the exchange rate had a positive effect on loans to the private sector, whereas the MPR and cash reserve ratio had a considerable negative influence. By using a Vector Error Correction Model (VECM) on yearly data from 1995 to 2021, this was found. The effects of inflation varied according on the duration of the time. The experts found that lowering policy rates may increase lending availability during economic expansion.

In a related study, Ibrahim and Mohammed (2021) looked at how changes in monetary policy rates affected the growth of loans in Nigerian deposit money institutions. The GDP growth rate (which was deemed independent), the inflation rate, the monetary policy rate, and the total quantity of bank loans to the private sector (which was deemed dependent) were the criteria that were looked at. The results showed a positive link with GDP growth but a long-term negative correlation between MPR and bank loans. The Fully Modified Ordinary Least Squares (FMOLS) method was used to arrive at these conclusions. According to the study, loan growth was more affected by changes in MPR than by changes in economic growth. Furthermore,

Nwafor and Okeke (2021) looked at the connection between Nigerian interest rate policy and bank loans. Commercial bank loans were the dependent variable, while the independent variables were the prime lending rate, the MPR, and inflation. MPR dramatically decreased bank loans over the short and long terms, although inflation had little effect on these results. The ARDL method was used to find this. The study comes to the conclusion that steady interest rates are necessary to get more bank loans.

Nwachukwu and Eze (2021) investigated how shifts in the policy rate affect the lending options available to Nigerian banks. They employed the MPR, interest rate spread, liquidity ratio, and non-performing loan ratio as independent variables. The dependent variable in the research was the total amount of bank credit. Using data for twenty Nigerian banks from 2008 to 2020 using the Generalised Method of Moments (GMM) estimate, the results showed that while lending capacity was supported by the liquidity ratio and interest rate spread, changes in the policy rate significantly affected the amount of money banks loaned. Credit availability is adversely affected by unpaid loans. The study's conclusions show that preserving policy rate stability enhances bank loan routes. Furthermore, Adeyemi and Musa (2020) looked at how Nigeria's monetary policy transfer mechanism affected the country's credit expansion. The money supply ratio (MPR), broad money supply, GDP growth rate, and exchange rate fluctuation were all unaffected by other factors. The amount of bank loans given to the private sector was the dependent variable. They utilised Structural Vector Autoregression (SVAR) to analyse quarterly data from 2000 to 2019 and found that while GDP growth led to an increase in credit, a one percentage point increase in MPR resulted in a substantial decline in private sector credit over the following two quarters. The lending market's response to policy changes was hampered by exchange rate fragility. According to their research, the credit channel of monetary policy works well, but because the macroeconomy is changing so quickly, consumers find it challenging to make plans.

Adekunle et al. (2020) looked at changes in Nigeria's monetary policy rate and loan flows from commercial banks. The money supply, MPR, inflation, and exchange rate were independent variables, whereas the total loans and advances were dependent elements. A study using the Generalised Method of Moments (GMM) found that the money supply has a positive and substantial impact on the credit supply. It became clear that changes in MPR had a significant impact on the results of extending credit in Nigeria. Yusuf and Bello (2020) also looked into how the Monetary Policy Rate affected bank lending in Nigeria. The cash reserve ratio, inflation rate, MPR, and loan interest rate were considered independent variables, while the amount of money that commercial banks lend was considered the dependent variable. The results of the Johansen cointegration test and the VECM showed that increases in the MPR make lending significantly more challenging, even while inflation has a beneficial short-term effect. According to the research, a steady MPR is necessary for long-term credit expansion.

Ibrahim and Lawal (2019) investigated how Nigeria's monetary policy tools affected the ability of private banks to distribute money. The MPR, liquidity ratio, and inflation rate were the independent variables, while the total amount of debt was the dependent variable. They found that MPR had a significant negative association with bank loans, the liquidity ratio had a little positive link, and inflation had no bearing. Ordinary Least Squares (OLS) analysis of yearly data from 1990 to 2018 was used to demonstrate this. The researchers found that interest-rate-based policies had a greater effect on bank lending than reserve limits. Eze and Odo (2019), on

the other hand, looked at "The Dynamic Relationship between Monetary Policy Rate and Loan Supply in the Nigerian Banking Sector." GDP, MPR, and the cash reserve ratio were the independent factors in their study, while the quantity of commercial bank loans was the dependent variable. They found that the long-term loan supply was significantly impacted negatively by the MPR, but positively by GDP growth. The ARDL limits test demonstrated this. The cash reserve ratio stopped loans from happening in the short and long terms. These results led them to believe that lowering the MPR and reserve requirements at the same time may encourage lending.

Musa and Danladi (2019) looked at how monetary policy affected the growth of loans in Nigerian banks. While bank loan growth was reliant, inflation, the Market Price Index (MPR), the exchange rate, and real GDP were independent. Based on the Structural Vector Autoregression (SVAR) model, the study's conclusions show that MPR shocks lead to sharp drops in credit growth, with a recovery taking place across many economic quarters. The authors came to the conclusion that the most important way to transfer money in Nigeria is still through the interest rate channel. Eboh and Chukwu (2019) also looked into how Nigeria's monetary policy and private sector lending operated. MPR, the money supply, inflation, and the liquidity ratio were considered independent variables, whereas private sector credit was considered the dependent variable. Over time, private sector loans are negatively impacted by inflation and MPR, according to the results, which were derived using OLS and error correction models. The finding was that the growth of loans is impeded by tighter monetary policy.

Johnson and Uche (2018) looked into how Nigeria's interest rate policy affects how many loans banks offer. The MPR, prime lending rate, and Treasury bill rate were the three independent variables. The quantity of bank credit given to the business was the dependent variable. The results showed that the prime lending rate had no effect on bank credit based on the ARDL calculation. However, the MPR and the Treasury Bill Rate had a major detrimental effect on bank credit. The research claims that while policy rates are high, borrowing remains challenging for the private sector. Oladipo and Afolabi (2018) reexamined the connection between the Monetary Policy Rate and bank lending in Nigeria's banking sector. The money supply, inflation rate, cash reserve ratio, and MPR were the independent variables, whereas a commercial bank loan was the dependent variable. The results showed that greater MPRs always lead to less bank loans, both immediately and over time. The ECM guess was used to find these findings. The study's conclusions indicate that Nigeria's monetary policy is still strict when it comes to lending.

Ogunyemi and Falade (2018) used commercial bank credit as the dependent variable in their study, "The Role of Monetary Policy in Influencing Bank Credit Allocation in Nigeria." The independent variables were the exchange rate, broad money, inflation, and the MPR. Using a technique called Fully Modified Ordinary Least Squares (FMOLS), they found that while loans were made easier by broad money and rising exchange rates, obtaining credit became much more challenging due to the MPR. Inflation had little effect. They came to the conclusion that an expansionary monetary policy helps the working sector since it promotes more loans. Yusuf and Bello (2017) looked into how interest rate strategy affected loans to small and medium-sized businesses in Nigeria. They employed the prime lending rate, GDP growth, inflation, and small business loans as independent variables and the MPR as a dependent variable. They looked at loans made to small and medium-sized businesses (SMEs) at fifteen different banks between

2005 and 2016 using panel regression. They found that while GDP growth helped SME financing, the prime lending rate and MPR made it more difficult. Actually, the impact of inflation was little. They came to the conclusion that lowering loan rates might help small and medium-sized businesses (SMEs) grow and create jobs. Finally, Okeke and Nnaji (2017) examined the connection between credit creation in Nigerian savings money institutions and monetary policy. The money market rate (MPR), reserve requirement, and interbank rate were utilised as independent variables and total bank credit as the dependent variable. Using VECM on quarterly data from 2000 to 2016, they found that market rates had a modest but beneficial influence on loan origination, whereas the MPR had a negative effect. The requirement for funds made it extremely difficult to get loans. They came to the conclusion that the MPR is essential for figuring out whether loans are available in Nigeria.

Gap and Adding Value

The empirical studies that were examined all examined the relationship between private bank lending in Nigeria and the Monetary Policy Rate. Other macroeconomic variables, including the rate of inflation, the exchange rate, the money supply, the GDP, the liquidity ratio, the cash reserve ratio (CRR), the interest rate spread, and the treasury bill rate, are sometimes included in these studies. The majority of research uses time series econometric methods, including panel Generalised Method of Moments (GMM) (Nwachukwu & Eze, 2021; Adek), Fully Modified Ordinary Least Squares (FMOLS) (Ibrahim & Mohammed, 2021; Ogunyemi & Falade, 2018), Autoregressive Distributed Lag (ARDL) bounds testing (Akinlo & Apanisile, 2023; Okonkwo & Uche, 2023; Nwafor & Okeke, 2021).

These studies consistently show that changes in MPR, especially increases, have a significant and detrimental long-term impact on commercial bank lending. This result implies that loan expansion is hampered by stricter monetary policy. The influence of several other macroeconomic factors varies. For instance, GDP growth often increases the likelihood of lending (Okonkwo & Uche, 2023; Ibrahim & Mohammed, 2021), while the effects of inflation and currency rates vary depending on the model parameter and the time period (Afolabi & Ogunleye, 2022; Adeyemi & Musa, 2020). The money supply tends to be positively correlated with lending (Adekunle et al., 2020; Ogunyemi & Falade, 2018), although reserve limitations (CRR, liquidity ratio) sometimes restrict credit supply (Okoye & Eze, 2022; Okeke & Nnaji, 2017). Lending and the money supply have a positive correlation, according to other research. Nevertheless, there are several clear limits and research gaps. First, the majority of the studies I've come across concentrate on either aggregate commercial bank lending or private sector credit. However, there is little research on lending by industry or company size (e.g., small vs large enterprises). This makes it challenging to understand how changes in the MPR impact various business types. Second, while many studies incorporate many monetary policy tools, they seldom look at potential interactions between MPR and other tools like CRR or liquidity ratio.

Third, only in extreme cases has policy rate volatility—which is distinct from level adjustments—been examined (Nwachukwu & Eze, 2021). As a result, there is a dearth of information regarding the stability component of monetary policy. Fourth, most evaluations employ linear models, which might not be able to capture the asymmetric effects of increasing vs decreasing the MPR on bank lending practices. Finally, while some studies employ panel bank-level data, the majority rely on macroeconomic time series. This limits the understanding

of the traits and risk profiles of certain institutions, which might play a role in the relationship between MPR and lending. Research that considers the volatility and asymmetry of policy rates, integrates data from bank-level panels with macroeconomic factors, and examines how various lending market sectors respond to shifts in MPR is therefore still possible. Such a strategy may lead to more in-depth policy insights on how Nigeria's banking industry transmits monetary policy through the lending channel.

Methodology

The Central Bank of Nigeria's (CBN) Statistical Bulletin, 2024, provided the secondary data used in this study. The Monetary Policy Rate (MPR), Inflation Rate (INF), Cash Reserve Ratio (CRR), and Liquidity Ratio (LQR) were the variables used to reflect changes in monetary policy rates between 1990 and 2024. In contrast, Commercial Bank Lending in Nigeria was represented by Total Credit to the Private Sector (TCPS). In this study, the Augmented Dickey Fuller Unit root and Auto-regressive Distributive Lag were used for the stationarity status and variable analysis.

Model Specification

The model of this study is based on the modification of Ademokoya et al (2020) when investigating the Impact of Monetary Policy on Bank Credit in Nigeria. Their model was;

$$LG = f(IR, GDP, CPI, CAP, LIQ) \quad (1)$$

Where: LG = loan granted, IR= change in interbank rate, GDP= gross domestic product, CPI = consumer price index, CAP = capital, and LIQ = liquidity.

Thus, the researcher adjusted the model to account for the inflation rate, cash reserve ratio, and monetary policy rate in order to accomplish the study's goal. Thus, the new enlarged model is expressed as follows;

$$TCPS = f(MPR, INF, CRR, LQR) \quad (2)$$

$$TCPS = \beta_0 + \beta_1 MPR + \beta_2 INF + \beta_3 CRR + \beta_4 LQR \quad (3)$$

$$TCPS_t = \beta_0 + \beta_1 MPR_t + \beta_2 INF_t + \beta_3 CRR_t + \beta_4 LQR_t + \mu_t \quad (4)$$

Where: TCPS = Total Credit to Private Sector, GCXE= Monetary Policy Rate, INF = Inflation Rate, CRR = Cash Reserve Ratio, LQR = Liquidity Ratio, μ = Error term, β_0 = Constant β_1 - β_4 = Estimated Parameters, **apriori expectation:** β_1, β_2 , and β_3 , >0 , $\beta_4 < 0$

Description of Variables in the Model

Total Credit to Private Sector (TCPS): In order to invest, consume, or participate in other economic activities, private enterprises, families, and individuals can borrow this money from lending organisations like banks. When compared to the public sector and the government, any entity that does not get loans, advances, or other types of credit is considered non-government. The study used an annual credit to the private sector (representing commercial bank lending) measurement in the millions of naira.

Monetary Policy Rate (MPR): The lending and deposit rates in the economy are influenced by this benchmark interest rate that the Central Bank of Nigeria has set. It aids in the management of both inflation and growth. Borrowing money becomes more expensive for individuals and businesses when commercial banks respond to a rise in the Monetary Policy Rate by raising lending rates. An increase in interest rates causes banks to be more cautious when extending loans, which decreases the demand for lending. Consequently, investment and consumption slow down, private sector credit diminishes, and the economy can take a hit overall. Since monetary policy rates are inversely connected to total credit to the private sector, this article's

central thesis is that this is the case. The monetary policy rate, expressed as a percentage (%), stands in for real changes in monetary policy in this study.

Inflation Rate (INF): represents the relative shift in the general level of prices across an economy over a certain period, usually a year. This reflects both the pace of price rises and the decline in purchasing power. As the inflation rate increases, prices for both consumers and businesses fall due to a decline in the buying power of the currency. As a result, private sector actors often have less ability to borrow and repay debts, as their profits and real incomes are reduced. Since private sector credit is already at record lows, an increase in inflation might have a chilling effect on investment and economic development. Therefore, it is anticipated that the total loan to the private sector will be negatively correlated with the inflation rate. In this case, changes in monetary policy are represented by the percentage-based inflation rate.

Cash Reserve Ratio (CRR): The Central Bank of Nigeria has ordered that a commercial bank maintain a certain percentage of its total deposits as reserves, rather than lending them out. When the Cash Reserve Ratio goes up, banks are compelled to retain a larger part of their deposits at the central bank, which limits the amount of money they may lend out. This reduces the amount of credit that may reach the private sector by making it more difficult for people and businesses to receive loans. Private investment and economic activity may be curbed for a long time if the Cash Reserve Ratio is high. The study's underlying hypothesis was that a higher cash reserve ratio would be associated with lower total private sector lending. Here, the cash reserve ratio % serves as a stand-in for monetary policy changes.

Liquidity Ratio (LQR): is the minimum required level of liquid assets held by commercial banks, including cash, treasury bills, and other approved government securities, relative to their net demand and time commitments. For short-term obligations like client withdrawals, it ensures that banks have sufficient funds on hand. A rise to the liquidity ratio makes banks hold more of their money in liquid assets rather than lend it out, which reduces the private sector's access to credit. If businesses and individuals are unable to borrow as much money as before, investment and consumption can suffer. The total credit to private sector should thus be inversely linked to the liquidity ratio. It is common practice to describe the liquidity ratio as a percentage in order to represent changes in monetary policy. Thus, $\beta_4 < 0$.

Result and Discussion

Unit Root Test

The study's time series data is checked for stationarity using the Augmented Dickey Fuller (ADF) unit root test. Here are the results from table 1 below:

Table 1: Augmented Dickey Fuller (ADF) Unit Root Test

Variables	Levels		First Difference		Order of Integration	P-value
	ADF Statistics	5% Critical Value	ADF Statistics	5% Critical Value		
LTCPS	-1.941735	-3.568379	-2.474851	-3.568379	I(1)	0.0000
MPR	-2.267864	-3.557759	-9.379445	-3.562882	I(1)	0.0000
INF	-1.697397	-3.557759	-5.597342	-3.562882	I(1)	0.0004
CRR	-2.158126	-3.557759	-6.300507	-3.562882	I(1)	0.0001
LQR	-3.228508	-3.557759			I(0)	0.0274

Source: Author Computation 2025* Level of significance at 5%

This study used Augmented Dickey-Fuller (ADF) unit root tests to verify that the variables were integrated in the correct sequence. You may view the results of these tests in Table 1, which is located below. Different variable integration orderings or a mix of I(0) and I(1) series were found in the results of the Augmented Dickey-Fuller (ADF) analysis. As shown by the ADF result, LTCPS, MPR, INF, and LQR all become stationary after differencing 1(1), even if LQR is stationary at levels 1(0). To examine the long-term connection between these variables, the Autoregressive Distributive Lag (ARDL) Bounds test of co-integration is a suitable choice under these conditions.

Co-integration Test

Table 2: ARDL Bound Test

Test Statistics	Value	K
F-statistics	7.297469	4
Significance	I (0)	1(1)
10%	2.75	3.99
5%	3.35	4.77
1%	4.76	8.67

Source: Authors computation 2025

According to table 2, there are long-term correlations among the variables since the F-statistic value of 7.297469 is more than the critical values for both the lower and upper bounds. We rule out the possibility of a short-term correlation and conclude that a long-term relationship is necessary. Accordingly, commercial bank lending is affected by changes in Nigeria's monetary policy over the long term.

Model Short- and Long-Term Estimation Outcomes

Table 3 below displays the outcomes of the relationship between the short- and long-term dynamics of model one.

Table 3: ARDL Short and Long-run Result for the Model

Short Run Coefficient				
Variable	Coefficient	Std. Error	t-Statistics	Prob
D((MPR(-1)	-0.114383	0.095635	-1.196047	0.2491
D(INF(-1)	0.030655	0.019897	1.540637	0.1429
D(CRR)	-1.106654	0.057030	-1.870124	0.0799
D(LQR)	-0.057074	0.016048	-3.556492	0.0026
ECM(-1)	-0.546347	0.185766	-2.941053	0.0096
Long Run Coefficient				
Variable	Coefficient	Std. Error	t-Statistics	Prob
D((MPR)	0.767931	0.281076	2.732115	0.0406
D(INF)	-0.303908	0.090707	-3.350443	0.0005
D((CRR)	0.323495	0.186433	1.735176	0.0946
D(LQR)	-0.486828	0.150481	-3.235147	0.0008
C	0.648276	0.211355	3.067238	0.0074
Adj R² = 0.445759, F-statistics = 2.794136 (0.027189), DW = 1.984271				

Source: Authors computation using E-view 13 2025

The coefficient estimate for the error correcting term, $ECM(-1)$, is negative at the 0.05 level of significance. This data suggests that, over the long term, the model will achieve equilibrium at a rate of 0.55% annually. From what we can see, a yearly adjustment speed of 0.55% might be precisely what we need to fix the error that happened last year. The R^2 number, which stands for modified R-squared, shows that MPR, INF, CRR, and LQR account for 45% of the variation in LTCPS, the dependent variable. At the 5% level of significance, the F-statistic is remarkable, hence every part of the model is interesting. According to the Durbin-Watson statistics of 1.984271, which is quite near to the value of 2, the model would not function without serial correlation.

Table 3 displays the model's short-term and long-term results. A negative and statistically significant link was seen between the logarithm coefficient of total credit to the private sector (LTCPS) and the liquidity ratio (LQR) in the near term. The cash reserve ratio (CRR) and the monetary policy rate (MPR) were determined to have a negative and statistically insignificant connection, however. Logarithm of total credit to the private sector (LTCPS) showed a positive correlation with inflation in the short term, but the correlation did not reach statistical significance. Even when the connection was favourable, this remained true. Tabulated in table 3 are the results of the long-run correlation between the logarithm of total private sector credit (LTCPS), the inflation rate (INF), and the liquidity ratio (LQR). In the end, this connection proved to be crucial. With time, a positive and statistically significant correlation was seen between the monetary policy rate (MPR) and the logarithm coefficient of total credit to the private sector (LTCPS). However, there was a positive, but non-significant, long-term correlation between the cash reserve ratio (CRR) and the LTCPS.

Diagnostic Test

Table 4: Ramsey Reset Test, Serial Correlation LM Test and Homoscedasticity Test Results

	F-Statistic	Prob-Value
Ramsey Reset Test	6.620513	0.0381
Breusch-Godfrey Serial Correlation LM Test	0.216510	0.8060
Breusch-Pagan-Godfrey Heteroskedasticity Test	1.426654	0.2690

Source: Authors computation 2025

Based on the diagnostic test results shown in Table 5, it is evident that the Ramsey Reset test was used to test for data linearity. The results showed that both the f-statistic (6.620513) and the p-value (0.0381) are more than the statistically significant threshold of 0.05. Based on their findings, the researchers rejected the null hypothesis and concluded that the model was accurately described. A chi-square probability value of 0.8060 and an f-statistic of 0.216510 were produced by the Serial or Autocorrelation Test, which was conducted with the Breusch-Godfrey Serial Correlation LM Test. It is clear from the investigation results that the model is free of serial correlation. This is due to the fact that the critical value of 5% (0.05) is exceeded by the probability value of about 63% (0.6331). The f-statistic was determined to be 1.426654 and the Chi-Square probability to be 0.2690 when heteroscedasticity was examined using the Breusch-Pagan-Godfrey technique. Since the probability Chi-square value is more than 5% ($P > 0.05$), the findings indicate that the model is free of heteroskedasticity. This means that the residuals have a constant variance and are homoscedastic, two desirable properties in regression.

Discussion of Findings

Monetary Policy Rate and Total Credit to Private Sector in Nigeria

The ARDL estimation reveals that the Monetary Policy Rate (MPR) exerts a positive and statistically significant influence on Total Credit to the Private Sector (TCPS), underscoring the potency of Nigeria's interest rate channel of the Monetary Transmission Mechanism Theory (Bernanke & Blinder, 1992; Mishkin, 1996). This suggests that rather than constraining lending, policy rate adjustments stimulate credit intermediation, reflecting the responsiveness of Nigerian banks to monetary signals in mobilizing loanable funds. Such evidence contrasts with dominant findings in empirical literature (e.g., Akinlo & Apanisile, 2023; Okonkwo & Uche, 2023), which emphasize a contractionary effect of high MPR on credit supply, but it highlights that under specific macro-financial conditions, monetary tightening can paradoxically strengthen banks' credit channels by attracting savings, enhancing liquidity, and expanding credit portfolios. The rejection of the null hypothesis therefore affirms that monetary policy in Nigeria significantly drives private sector credit, validating the relevance of interest rate dynamics in shaping credit markets.

Inflation Rate and Total Credit to Private Sector in Nigeria

The ARDL analysis reveals that inflation exerts a negative and statistically significant effect on total credit to the private sector in Nigeria. This aligns with the Monetary Transmission Mechanism Theory (Bernanke & Gertler, 1995), which posits that rising inflation erodes real lending capacity by tightening liquidity conditions, raising risk premiums, and discouraging credit expansion. Empirically, Eboh and Chukwu (2019) similarly found that inflationary pressures depress private sector credit in the long run, underscoring the crowding-out effect of price instability on bank intermediation. By rejecting the null hypothesis, the result confirms that inflationary dynamics remain a critical constraint to credit growth, reinforcing the view that macroeconomic stability is a prerequisite for a vibrant credit market.

Cash Reserve Ratio and Total Credit to Private Sector in Nigeria

The ARDL results reveal that the Cash Reserve Ratio (CRR) bears a positive but statistically insignificant relationship with credit to the private sector, suggesting that reserve requirements in Nigeria do not meaningfully influence banks' lending capacity. Within the lens of the Monetary Transmission Mechanism Theory (Bernanke & Blinder, 1992; Mishkin, 1996), this insignificance implies that the credit channel is weak, as higher reserves neither crowd out nor expand loanable funds in a measurable way. Empirically, this finding resonates with Ibrahim & Lawal (2019), who observed that interest rate-based tools dominate CRR in shaping bank lending, underscoring that in Nigeria's context, reserve requirements function more as a liquidity-mopping instrument than a driver of credit creation.

Liquidity Ratio and Total Credit to Private Sector in Nigeria

The ARDL findings indicate that the liquidity ratio (LQR) exerts a negative and statistically significant impact on credit to the private sector, implying that higher liquidity holdings crowd out loanable funds and constrain banks' intermediation role. This aligns with the Loanable Funds Theory (Wicksell, 1898; Ohlin, 1937), which posits that excessive reserve accumulation reduces the supply of credit available to borrowers, tightening financial conditions. Empirically, Eboh and Chukwu (2019) confirm that monetary tightening through liquidity requirements suppresses private sector credit, highlighting the sensitivity of Nigerian banks' lending behaviour to prudential ratios. Thus, rejecting the null hypothesis underscores that liquidity regulation significantly shapes credit supply in Nigeria.

Conclusion and Recommendation

Conclusion

According to studies that looked at the link between monetary policy changes and commercial bank loans, total private sector credit was positively and significantly correlated with the monetary policy rate, but negatively and significantly correlated with the liquidity ratio and inflation rate. Although the cash reserve ratio is positively correlated with total private sector lending, the association is not statistically significant. A detrimental effect of monetary policy shifts on commercial bank lending and the Nigerian economy was thus established.

Recommendations

- i. The Central Bank of Nigeria (CBN) should continue to adopt a balanced interest rate framework that encourages credit expansion without fueling excessive inflation, thereby supporting sustainable private sector growth.
- ii. National Bureau of Statistics (NBS) and Federal Ministry of Finance should strengthen inflation-monitoring systems and enforce policies that stabilize prices, ensuring a conducive environment for credit expansion.
- iii. Central Bank of Nigeria (CBN) should reconsider the effectiveness of CRR as a policy tool and instead complement it with more direct credit-support mechanisms, such as targeted refinancing schemes for priority sectors.
- iv. Finally, the Nigerian Deposit Insurance Corporation (NDIC) and Federal Ministry of Budget and National Planning should re-evaluate prudential ratios to strike a balance between financial stability and lending capacity, encouraging banks to channel more funds toward productive private sector investment.

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